

**WEST BANK AND GAZA:
INDUSTRIAL ESTATE DEVELOPMENT**

**NEXT STEPS AND POSSIBLE
ROLES FOR USAID SUPPORT**

Final Report

U.S. Agency for International Development

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ACRONYMS AND ABBREVIATIONS

| | |
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| ANERA | American Near East Refugee Association |
| DOP | Declaration of Principles |
| EPZ | Export Processing Zone |
| ERP | Emergency Rehabilitation Project |
| FIAS | Foreign Investment Advisory Service |
| FTA | Free Trade Agreement |
| GDP | Gross Domestic Product |
| G/EG/EIR | Bureau for Global Affairs, Center for Economic Growth, Office of Economic and Institutional Reform |
| GOI | Government of Israel |
| ha | hectare |
| km | kilometer |
| IE | Industrial Estate |
| MIGA | Multilateral Investment Guarantee Agency |
| OPIC | Overseas Private Investment Corporation |
| PA | Palestinian Authority |
| PADICO | Palestine Development and Investment Company, Ltd. |
| PECDAR | Palestinian Economic Council for Development and Reconstruction |
| PD-20 | USAID Policy Determination Number 20 |
| PEDS III | Private Enterprise Development Support Project (Phase III) |
| PIEA | Palestinian Industrial Estate Authority |
| PLO | Palestine Liberation Organization |
| sq. ft. | square foot |
| sq.m. | square meter |
| TATF | Technical Assistance Trust Fund |
| TSG | The Services Group |
| USAID | United States Agency for International Development |
| VAT | Value Added Tax |
| WBG | West Bank and Gaza Strip |

CONVERSION RATES:

US\$1 = 2.91NIS

1 dunam = 1,000 sq.m.

1 ha. = 10,000 sq.m.

1 sq.m. = 10.762 sq.ft.

Introduction

This study has been prepared by The Services Group (TSG) under subcontract to Coopers & Lybrand, in fulfillment of a Task Order Request under the Private Enterprise Development Support Project III (PEDS III) with the U.S. Agency for International Development (USAID). This report is a review of the proposed Industrial Estate (IE) development program in the West Bank and Gaza (WBG). Its purpose is to review the progress made to date on the development of IEs in WBG, identify the primary issues outstanding, examine the legal implications of U.S. assistance to such a program, and provide guidance to the USAID Mission to the West Bank and Gaza about its possible role.

This analysis is based on a series of meetings and discussions held in Israel and the West Bank and Gaza, as well as, a review of the documentation prepared by the World Bank and other sources on the subject. Moreover, several briefings were held in Washington with World Bank personnel and representatives from the U.S. Departments of State and Commerce prior to traveling to the region.

Following this introductory section, this report is organized according to the following framework:

- Chapter II presents an overview of the industrial estate development program in the West Bank and Gaza. This section provides the contextual framework for the study, outlining the program's overall concept and objectives, reviewing its current status, and lastly, identifying the primary issues still outstanding.
- Chapter III reviews the provisions of Section 547 (b) of the Foreign Appropriations Act of 1993, prohibiting US assistance to the development of export processing zones (EPZs), as well as USAID's Policy Determination 20 (PD-20) of January 3, 1994. The objective of this Chapter is to provide technical input about the potential for U.S. job loss due to the development of the industrial estate program in the West bank and Gaza.
- Chapter IV provides an overview of the types of assistance that USAID could undertake to move the program forward. These tasks are broadly grouped into program activities and project-specific support, the former including such areas as institutional and regulatory support, as well as investment and

export promotion; and the latter including direct support to individual estate projects in the areas of feasibility studies, project finance, infrastructure funding, and the like.

- Chapter V presents the conclusions and recommendations, highlighting the major findings, and providing a summary on how USAID should proceed regarding the implementation of the program and what types of assistance should be offered.

This report has been prepared by a team of three experts, including Torge Gerlach, a TSG Vice President, Harold Pohoresky, an associate consultant with TSG, and Grant Morrill, Private Sector Officer, G/EG/EIR, at AID/Washington's Global Bureau. Messrs. Pohoresky and Morrill spent from May 29 to June 15, 1995 in the area, while Mr. Gerlach was in-country from June 6 - 15, 1995. The team was in-country to conduct first-hand discussions with USAID/WBG staff, U.S. Embassy personnel, and relevant representatives from the Government of Israel (GOI), the Palestinian Authority (PA), and private sector individuals in Israel and the territories under PA control and authority.

The team would like to thank the U.S. Ambassador to Israel, Mr. Martin Indyk, and the USAID/West Bank and Gaza Mission Director, Mr. Christopher Crowley, for the guidance and invaluable input during the mission, as well as the numerous other individuals that contributed to the findings of this study. The findings and conclusions of the report are, however, those of TSG and do not necessarily represent the views of USAID/WBG, Embassy personnel, AID/Washington, or other parties consulted during the course of the study.

Overview of Industrial Estate Development Program in the West Bank and Gaza

This chapter provides an overview of the primary issues surrounding IE development in the West Bank and Gaza. It begins with an overview of the background and the economic context of industrial estate development in the territories before reviewing the current status of the program and the work conducted to date. Finally, the chapter examines the primary issues surrounding the development of IEs in the WBG and outlines the steps toward successful implementation of such a program in the territories.

Background and Economic Context

Overview

Since the early 1980s, the West Bank and Gaza economies have more or less stagnated, constraining industrial development, largely due to labor out-migration. While the private sector has long been the dominant actor in the WBG, accounting for nearly 85 percent of GDP in 1991, the level of sophistication remains relatively low and unemployment high, and the general level of industrialization is disproportionately low compared to similar economies. Nevertheless, the fact that the private sector has managed to survive at all is testimony to the strong entrepreneurial spirit found in the indigenous Arab population. Almost two years ago, following the September 1993 signing of the Declaration of Principles (DOP), hopes were high that peace would lead to an improvement in living conditions and spur economic development. For a number of reasons, living conditions have deteriorated rather than improved, unemployment has increased and hope is beginning to diminish. A continuation of this trend may jeopardize prospects for sustainable peace.

There is a need for concerted efforts to reverse this decline. Politically, a number of events have taken place in the past two years to prepare for the full transfer of authority over the territories to the Palestinian Authority. Specifically, the following agreements have been reached:

- the DOP signed in Washington in September 1993 between Israel and the PLO;

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- the Protocol on economic relations (Paris Protocol) signed in April 1994; and,
- the Agreement on the Gaza Strip and the Jericho area (the Cairo Agreement), signed in early May 1994.

As of June 1, 1994, Gaza and Jericho were granted autonomy except for military and foreign affairs, for part of foreign trade and monetary policies and for a number of issues to be agreed upon during the permanent status negotiations. As of December 1, 1994, responsibility in the West Bank for health, education, social welfare, tourism and direct taxation had been transferred to the PA. While this progress is remarkable, there are still over 30 "spheres", or administrative responsibilities, that have yet to be transferred to the PA. Moreover, Jordan and Israel signed a peace agreement in late 1994, and preparations are underway for a first phase of direct talks that could lead to a peace agreement between Israel and Syria to be held in Washington in late June 1995.

To cement the success of the peace process on the political level, economic prosperity is crucial and a range of assistance activities has been initiated by the international donor community. Donors established the Holst Fund to support recurrent costs of the Palestinian Authority, and the Technical Assistance Trust Fund (TATF) to support priority technical assistance requirements. The World Bank (with donor cofinancing), has approved an emergency rehabilitation project (ERP) focusing on infrastructure rehabilitation and is preparing others, one supporting health and education and at least one including support for private sector development. Many donors have bilateral programs through which they are supporting a variety of activities.

Economic prosperity and development in the Palestinian territories will depend on continued progress in reaching satisfactory permanent agreements with Israel, as well as progress in creating a stable and attractive economic framework by the Palestinian Authorities. Recent World Bank documents have outlined the following areas which need to be addressed to stimulate private sector development and economic growth:

- Political risk mitigation to help protect against the uncertain political, security, and legal situation;
- Legal and regulatory reform to overcome the lack of clarity, modernize the antiquated legislation currently in place, and strengthen the enforcement capacity of the PA;

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- Financial sector reform to develop formal sources of credit, develop capital markets, etc.;
- Development of trade agreements and standardization of product design and quality;
- Development of investment promotion, as well as, regulatory institutions.;
- Small business support programs and support to Chambers of Commerce, as well as general business support services;
- Labor markets and training to overcome high rates of unemployment, and to address the weakness of vocational training and educational systems;
- Infrastructure development, particularly in areas critical to private sector development, such as telecommunications, power, water and sewerage, and transport; and,
- Industrial estate development to redress the lack of serviced industrial land and introduce a coordinated approach to industrial development, minimizing the detrimental environmental impact of enterprises locating in residential areas, while encouraging and support new investment and job creation.

While a detailed review and analysis of all of the factors raised above goes well beyond the scope of this report, the following is more detailed overview of the objectives and goals underlying the proposed industrial estate development program.

| | |
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| Industrial Estate Program Objective and Goals | The development of an industrial estate program will address several different objectives. In general terms, the program would overcome the following obstacles to economic growth: (i) lack of serviced industrial land; (ii) security concerns regarding the transit of Palestinian workers into Israel; (iii) problems in the timely movement of goods between the PA territories and Israel; (iv) high rates of unemployment; and, (v) the lack of a cohesive legal and regulatory framework for private sector development in general, and investment regulation in particular. Moreover, the IE program could mobilize capital from overseas Palestinian investors. Each of these issues is discussed in more detail below: |
|--|---|

- ***Lack of serviced industrial land.*** There is a lack of industrial land equipped with basic minimum infrastructure, such as utility hook-ups and access to the road network, in both the West Bank and Gaza Strip. Under Israeli occupation, development of the territories was discouraged for security and control reasons and very little land development was approved outside the municipalities. The Israeli Civil Administration has kept tight control over the existing industrial estates, such as the Erez Industrial estate just inside the Green Line on the northern-most border of the Gaza Strip. Due to the limited approvals given under Israeli occupation to develop industrial sites, land prices inside the municipalities skyrocketed, often to the point of arresting industrial development. In Gaza, the scarcity of land in general, combined with distortions in land markets, general lack of infrastructure, and other constraints has driven land prices to extreme heights. Land in municipalities in the West Bank and in industrial zones in Gaza sells for as much as \$250,000 per dunam, or \$250 per sq.m. (approximately \$25/sq.ft.), often raising overall development costs above an economic level.

The development of industrial estates will contribute to the pool of serviced land, and offer an alternative to the high-cost land near the municipalities, by allowing for the development of these estates in more remote locations. The proximity of the site to a large pool of readily available labor is not a major concern in the case of the WBG, as it generally is in locational analyses, due to the limited size of the territories. Moreover, the extremely high rates of unemployment will force people to relocate or commute to more remote areas if necessary to find employment.

- ***Security concerns regarding the transit of Palestinian workers into Israel.*** Prior to the peace agreement, there were as many as 120,000 Palestinian workers employed in Israel (1987 estimate). This number declined to approximately 85,000 in 1993, and less than 50,000 before the recent closures. These numbers have now fallen even further as Palestinian labor migration has been blocked by the closures, and Israeli business has replaced this source of labor with other foreign workers. The current estimate of the number of foreign workers, mostly from Thailand, Romania, Poland, and Turkey, is 90,000. At the same time, the unemployment rate in the WBG is now over 50 percent.

The creation of industrial estates in the territories could address this problem by relocating some of the jobs to where the workers are, rather than moving the workers to the jobs. Higher wage rates in Israel (by a factor of two) over the Palestinian territories, coupled with the shortage of Israeli laborers willing to work in low skill jobs, will lead to the shift and expansion of some industrial activities from Israel to the IEs in the WBG. This transfer of economic activity will lead to new job creation in the territories and a slowdown in the "importation" of foreign workers into Israel.

- ***High rates of unemployment.*** The industrial estate program will address the perhaps most pressing issue: high unemployment in Gaza (estimated at well over 50 percent and rising steadily) and the West Bank (30 percent). If properly designed, administered, and managed, the IEs would provide an attractive investment environment for Palestinian, Israeli, and foreign investors, who are looking to take advantage of the low-cost environment, as well as the opportunities to tap regional markets brought by the peace process.
- ***Lack of a cohesive legal and regulatory framework.*** As outlined in other sections of this report, the legal and regulatory environment in the WBG is inadequate and will need to be reformed and enforced. This is often a lengthy process, especially given the still uncertain outcome and provisions of the permanent agreement to be reached in the next four years. While the PA is working on creating a stable environment for local and foreign investment in the territories, a process which is likely to take years, the industrial estates will operate under a regime, which will address a number of the common concerns and uncertainties currently associated with investing in the region. As such, the program would fast track the necessary legal and regulatory clarification and reform, and mitigate political and security risks.
- ***Improve security arrangements for the transfer of merchandise between Israel and the PA territories.*** Depending on the final arrangements between the PA and the Government of Israel (GOI), the industrial estates could also provide a means to allow uninterrupted transit of goods from the WBG to Israel, even in the case of continued closures. If properly designed, the IEs along the green line could serve as a conduit for the transit of merchandise and services to Israel via a dedicated "gate" or "corridor".

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Security control systems should be included in the IE program establishing checkpoints within the estates to facilitate this traffic, even when the border is otherwise closed.

- ***Mobilize capital from overseas Palestinians.*** Lastly, the industrial estate program could mobilize the capital, know how, and international connections of overseas Palestinians for investment in relatively stable and secure sites. Currently, overseas Palestinian businesses face major restrictions and uncertainties, which inhibits their interest in investing in the WBG. Establishing appropriate guarantees and incentives for them under the estate regime should mobilize substantial capital and share expertise in support of development of the WBG, and the region in general.

Given the benefits listed above that the IE program is likely to achieve, the PA, the GOI, and the international donor community have each ascribed a high level of importance and commitment to the development of the program. The following is a review of the current status of the program's implementation and the work conducted to date.

Review of Current Status and Work Conducted to Date

World Bank Studies and Support

The World Bank has undertaken a number of studies and investigations relating to Private Sector Development (PSD) in the WBG in general, and the creation of an Industrial Estate program in particular. A paper circulated by the World Bank's Private Sector Development Office on March 23, 1995, entitled ***"West Bank and Gaza: Framework for Private Sector Development and Support"*** outlined a general strategy for World Bank support for private sector development in the territories. The paper included a review of the possibilities of establishing IEs and recommended continued support to this type of activity. The Foreign Investment Advisory Service (FIAS), a joint facility of the International Finance Corporation and The World Bank, issued a paper in April 1995 entitled ***"West Bank and Gaza: Creating a Framework for Foreign Direct Investment"***, which also included a discussion on the merits of an industrial estate program to address some of the infrastructural shortcomings identified and stimulate foreign direct investment in the region.

Most important perhaps is the detailed ***"Industrial Estates and Enabling Environment for Private Sector Development for West Bank***

and Gaza" prepared by a World Bank team, which conducted a project identification/pre-feasibility mission to the West Bank and Gaza to investigate the possibilities of creating an IE program. The document, which was just recently circulated includes detailed review of the following issues: (i) the legal, incentive and institutional frameworks for industrial estates; (ii) financial considerations in industrial estate development; (iii) a preliminary market survey of potential investors of border IEs; (iv) a review of proposed sites for industrial estates; (v) a project concept note for future World Bank project support; (vi) an outline of a proposed trust administered by the Multilateral Investment Guarantee Agency (MIGA); and (vii) a terms of reference for the appointment of consultants for the study of the development of industrial complexes in the WBG. This document examines the viability of an IE program in the WBG, across the dimensions noted above, and arrives at the conclusion that such a program makes sense economically provided the political conditions remain appropriate and the cooperation of all parties, including the donors, is forthcoming.

The World Bank report recommends the following urgent steps to start the process for border and local estates: (i) form a working group of all parties including donors to study and review the findings of the report; (ii) establish a committee to design and agree upon a comprehensive enabling environment with technical assistance from donors to facilitate the design process; (iii) finalize the selection of first phase sites and, for the PA, approve the terms of reference and finalize feasibility studies for these sites; (iv) for the municipal complex or very small industrial parks, constitute a counterpart group involving the Palestinian Ministry of Economy, the municipalities, ANERA, and Chambers of Commerce, finalize the terms of reference for the feasibility study, and approve its financing from the technical assistance trust fund or other appropriate sources.

While the World Bank paper represents the first step in seeking Bank approval for a large-scale Bank-supported project, it is unclear as of the time of this writing what the exact nature of Bank support and funding to the WBG IE program will be. It is clear, however, that the Bank would welcome the involvement of other donors in all aspects of program development. Close coordination between the Bank and USAID (as well as other donors) is therefore crucial at this stage of program development.

GOI/PA Joint Concept Paper The GOI and the PA have developed a joint concept paper which seems to generally follow the program outlined in the World Bank documents. This paper has served as the basis for negotiations to date, and focuses on some of the main issues in developing an

industrial estates program. The Israelis have reportedly approved the paper and are currently awaiting the signature of the Chairman of the PLO.

The paper makes reference to plans for developing nine zones in the territories under Palestinian jurisdiction: three in the Gaza strip and six in the West Bank. It is envisaged that the border sites will be geared to the needs of larger, export-oriented investors, while the interior sites will be geared to the needs of small- and medium-sized investors with the hope that backward and forward linkages can be developed between them. The private sector will develop and operate the parks. Estimates for the range of sizes for the various parks are 500 and more dunams for the larger ones, and 200 or less for the small and medium sized ones. Estimates also suggest that up to 20,000 jobs can be created in the near term (3 to 5 years) and 100,000 jobs in the longer term.

The paper also addresses infrastructure development requirements. Cost estimates for infrastructure development range from \$20 to 25 million per zone. The paper does, however, suggest that international donor involvement in developing the off-site infrastructure, linking the sites to the regional grids, should be sought. Cost estimates for this type of investment ranges from as low as \$5 million to \$15 million depending on the site characteristics.

Furthermore, the concept paper outlines the key elements to include in the legal, regulatory, and institutional framework to provide the basis for the operation of industrial estates. Other issues identified in the concept paper as basic requirements to assure the success of the IE program include: (i) the need for a political risk insurance scheme without which foreign investors would not invest; (ii) the need for customs exemption and preferential treatment for goods and services originating from the zones, in the form of free trade agreements with the U.S. and Europe; and (iii) a range of incentives to attract investors to the parks, the foundation for which is laid in the new investment law. Finally, the concept paper suggests that feasibility studies for the estates should start immediately and implementation of the program begin within the next six months.

The objective of the concept paper is for the PA and the GOI to agree on a plan of action with timetables and responsibilities which will then be presented to the international donor community at the Consultative Group meeting in Paris on July 10, 1995. At this session, project proponents will seek support from the donor community in developing the program. Support can take two forms:

(i) financial assistance for the development of the estate facilities (the "hardware"); and, (ii) technical assistance in finalizing the institutional and regulatory framework for the industrial estate program ("software").

While the concept paper outlines the general principles underlying the IE program in the West Bank and Gaza, it is not very detailed and provides little insight into fundamental issues underlying the successful development of the program. No progress seems to have been made in terms of agreeing upon regulatory framework under which the program would operate. These issues need to be addressed without further delay to build upon the present momentum and take advantage of private sector interest in the program.

Site Selection

A number of sites have been identified along the border between Israel and the West Bank and Gaza for border industrial estate development. The most promising of these in terms of support from both the PA and the GOI, land availability, location, and other basic site selection criteria are: Jenin and Hebron (Targumiya), in the West Bank; and Carni and the expansion area of the Erez industrial site in the Gaza Strip. Other sites, further inland than the border sites, have been earmarked for local development. These include Nablus, Bethlehem, and Kharbata in the West Bank, and Beit Hanoun and Deir al Balah in the Gaza Strip.

There is interest from a number of private sector groups in developing some of the border estates, as soon as agreement is reached on certain outstanding issues, such as legal framework and other agreements between the GOI and PA are finalized. The most active of these groups is PADICO, a holding company, consisting of mostly overseas Palestinian investors. PADICO has obtained preliminary concessions to develop both the Carni and the new Erez sites. In Carni, PADICO has been licensed to develop an initial area consisting of 500 dunams, with options on neighboring land, allowing the site to expand by an additional 2,000 dunams. PADICO is only awaiting donor funding for the off-site infrastructure to commence the simultaneous development of on-site facilities with its own financing. PADICO has also been selected to develop a new 200-dunam expansion of the Erez industrial site, and is awaiting final clarification on the authority over the land in question. Even though situated inside the Gaza Strip, the land is currently under the control of the Civil Authority of the GOI. Proposals for turning the land over to PA control prior to the expiration of the Cairo Agreement in 1999 are being reviewed, and PADICO is awaiting the outcome of those discussions before undertaking any site development.

Another group of private investors has been formed to develop the Jenin site. This group consists of Palestinian industrialists and bankers, who have purchased 500 dunams of land, with planned expansion of up to 1,000 dunams. The site is located only 40 km from the port city of Haifa and 30 km from Jordan making it a strategic location for manufacturing for export, both to Jordan and other export markets, such as Europe.

The current state of site planning for any of the proposed sites is unclear. It appears that no detailed feasibility studies have been undertaken for any of the sites, and a number of the private developers are looking for funding to defray the cost of these studies. Officials from the Civil Authority claim that feasibility studies for the development of the new Erez site have been finalized and construction could proceed without further delay.

The Palestinian Investment Act

The Palestinian Investment Act was signed into law by Chairman Arafat on April 30, 1995. Based on a brief review of the law, it falls short of international standards, particularly in terms of the competitiveness of the investment framework it sets in place. While a full review of the law goes beyond the scope of this study, the following is a brief summary of the primary concerns it raises.

The Act creates a new public agency, the Palestinian Higher Agency for the Promotion of Investment (PHAPI). The law stipulates that the Agency will be managed by a 15-member Board of Directors, consisting of nine PA Ministers, two representatives from the Chambers of Commerce and industry, and four private sector members, appointed by the President of the National Authority? The organization's large, public sector board is a departure for current best practice worldwide in investment promotion, which is increasingly private-sector in orientation. Experience has shown that a lean organization with heavy private sector involvement will be more effective in meeting its objectives. Moreover, the agency has the dual roles of promoting, as well as regulating investment, while the prevailing trend is toward separation of these potentially conflicting functions between different agencies.

Lastly, the Act extends investment incentives which seem to be largely based on the Israeli law. As such the law divides the PA territories into areas "A, B, and C," where tax holidays ranging from two to five years are provided, depending on the location. While this is similar to the Israeli system, it is less competitive, as the Israeli Government also provides a host of other incentives such as cash grants for capital investment. Given that the PA is in no position to

grant similar incremental incentives, additional attention should have been given to the base package of incentives established in the Act.

The Industrial Estates Law

According to a high-ranking official in the PA, a first draft of the Industrial Estates Law has been prepared. Unfortunately, a copy was not made available to the team during the mission. Most likely the law will focus on the creation of the Palestinian Industrial Estates Authority and provide some additional incentives to investors in the estates. Given the concerns already raised regarding the Investment Act, it would be prudent to provide assistance to the PA in finalizing the industrial estates law as soon as possible.

Outstanding Issues

While significant progress has been made in advancing the Industrial Estate Program, a number of issues were identified by the team that remain to be addressed. The following list is not an all-encompassing, but rather highlights those items that are most important to the USAID mission to the West Bank and Gaza in determining its future involvement in the program and in designing a possible assistance project.

- **Continued Uncertainty over Security Measures.** The PA and GOI have yet to agree on the security controls of the border industrial estates. The viability of the program will be jeopardized if Israel continues the practice of "closures" in response to terrorist actions. While the security concerns of Israel are legitimate, and the GOI has the right and responsibility to protect its citizens, the industrial estate program cannot function without the guaranteed transfer of goods and merchandise in and out of Israel. At a minimum, the PA and the GOI have to agree on a framework that will allow for the free transfer of merchandise from the industrial estates into Israel, even in the case of border closures. This could be achieved by implementing security procedures and establishing checkpoints within the border IEs. Additionally, assistance to the PA to obtain a commitment from the GOI to ensure free passage of goods will be desirable. This is one of the fundamental requirements for the economic viability of the companies in the Industrial Estates.
- **Lack of Clear Regulatory and Institutional Framework.** While private sector interest in developing IEs in the West Bank and Gaza appears to be strong, future tenants of the estates will be less forthcoming in the absence of a clear legal environment. One of the underlying objectives of the program is to fast-track the legal and regulatory reform required in the territories, and mitigate political and security

risks. The proposed IE program is designed to overcome some of the shortcomings of the legal environment in the WBG and a solid foundation has to be developed under which the program will operate.

- **Creation of the Industrial Estate Authority.** Whether a separate entity or a ministerial department, there is a clear need for an agency to administer the legal, regulatory, and incentive regime, plan the overall industrial estate program, and promote investment by developers and tenants. Several factors make the establishment of an industrial estate authority a necessity. First, a legal entity must be vested with the authority delegated on behalf of the PA and Israel. Second, the regime of incentives, security and other arrangements for the estates requires effective coordination and responsive administration. Third, there is limited capacity within the PA to handle such responsibility directly, as part of other routine industrial regulation activities. A small, agile, tightly focused organization is needed for a rapid start up and long-term effectiveness. Given the complex nature of the Investment Authority established through the new Investment Act, there is great concern over the PA's ability to create a lean and effective agency to administer the estates program.
- **Need for Coordination and Planning of Industrial Estate Development.** In the absence of an overall Industrial Development Plan, careful planning and phasing of industrial estate development is imperative. The results of the market survey conducted for the World Bank are positive, and suggest high demand for space in the estates. However, the survey scope was limited and there has not been a full-scale market demand assessment that would justify the development of nine industrial estates. It is not even clear that development of more than one IE each in the West Bank and in Gaza is justified at this time. The World Bank Study *"Industrial Estates and Enabling Environment for Private Sector Development for West Bank and Gaza"* recommends that a program-wide feasibility study be carried out. A detailed terms of reference is included as Annex 10 to the report, outlining the scope of a study, which would further refine the configuration of the estates program, and test its competitiveness in the international business environment. The findings of this study will be invaluable in designing the program and provide input into the phasing of IE development in the WBG.

- **Protection of Environmental, Health and Safety, and Labor Conditions.** Another issue, which relates directly to the overall legal and institutional framework for the IE program, is the concern over basic environmental, health and safety, and labor conditions. The Erez industrial area serves as an example of what may happen in the absence of clear guidelines and regulations regarding these issues. The area is poorly maintained; trash and litter are scattered throughout the estate. Minimum standards must be set and criteria applied to assure the future of the estates, as well as international donor support. Once drafted, these regulations could be enforced by the industrial estates authority mentioned above.
- **Firm Commitment to the Success of the Industrial Estates Program.** While there appears to be strong support to develop IEs in the WBG among the PA, the GOI, the Israeli and Palestinian private sector, and the international donor community, future commitment to the program must be assured. Most importantly at this juncture is the commitment and support of the PA and the GOI in developing the requisite agreements and regulations to make the program work. Equally important will be the support of the international donor community, both in providing funding for physical infrastructure development and in providing the technical expertise required to design the program and the legal, regulatory, and institutional framework under which the program will operate. The concerned parties must work together very closely and make sure that the momentum continues.
- **Clear Delineation of Responsibilities Under the Program is Needed.** Once the joint concept paper is circulated, and agreement reached on its general principles, the PA, the GOI, and the donors should form a task force or working group, consisting of a limited number of representatives from the key groups, to work out the details of the program. Currently, no one group is moving the process forward, which will ultimately hinder the process and slow down the progress being made.

Regardless of the final outcome of further studies and the eventual configuration and scope of the industrial estate program in the WBG, there is a clear need for a proper legal and regulatory framework to promote economic and industrial development in the territories.

Impact on U.S. Jobs

This Chapter provides a discussion of the West Bank and Gaza industrial estate program and USAID's Policy Determination PD-20, issued by USAID in January 1994. The Chapter attempts to review the concepts of the proposed industrial estate program in light of the provisions of PD-20 and reviews the potential for job loss in the United States due to the development of an industrial estate program in the WBG.

Summary and Intent of the Act

In the fall of 1992, the FY 1993 Foreign Operations, Export Financing, and Related Programs Appropriations Act was adopted by Congress. The Act prohibits:

- use of funds appropriated by the Act to provide financial incentives to a U.S. business to relocate its operations outside the United States;
- provision of assistance for the purpose of establishing an export processing zone, or designated area, in a foreign country, in which the tax, tariff, labor, environment and safety laws of that country do not apply; and,
- assistance for any project or activity that contributes to the violation of internationally recognized workers rights.

Section 547 of P.L. 103-87 continued this prohibition for FY 1994, except that subsection (c) was modified to exempt the informal sector, micro and small scale enterprises, and smallholder agriculture. In November 1992 USAID/W issued policy guidelines stating that all USAID missions were to review their project portfolios and to phase out projects that are in violation of the provisions of Section 599, regardless of the year the project was originally funded. The final guidelines regarding the legislation were issued on January 3, 1994 as Policy Determination 20.

Section 547 of the Foreign Appropriations Act states, in pertinent part, as follows:

~~None of the Funds appropriated by this Act may be obligated or expended to provide:~~

- (b) *Assistance for the purpose of establishing or developing in a foreign country any export processing zone or designated area in which the tax, tariff, labor, environment, and safety laws of that country do not apply, in part or in whole, to activities carried out within that zone or area, unless the President determines and certifies that such assistance is not likely to cause a loss of jobs within the United States.*
-

Potential Impact on U.S. Jobs

Background

As U.S. labor costs increased in the post-war period, lower-skilled, labor-intensive industries in the United States became increasingly less competitive. Reacting to competitive pressure, manufacturers, especially apparel, have reduced their costs by moving labor-intensive assembly operations to offshore locations. During the 1970s and 1980s countries in the Caribbean Basin especially saw a large influx of U.S. assembly operators. The U.S. Government, under the Caribbean Basin Initiative (CBI) encouraged such activities by providing incentives if U.S. made parts were assembled in the Caribbean, and the finished product shipped back to the United States.

Many countries in the region saw this opportunity for attracting large numbers of U.S. investors and offered export incentives, such as tax holidays, tariff and duty exemptions, and other provisions through a number of national export processing zone regimes. The Dominican Republic, El Salvador, Honduras, Costa Rica, and Jamaica were especially aggressive in offering these types of incentives to attract large numbers of light assembly operations into their respective free zone programs. Coupled with significantly lower wage rates and close geographic proximity to the end market, these countries became attractive investment locations for U.S. manufacturers looking for alternative, lower cost manufacturing sites.

The U.S. Government, through the U.S. Agency for International Development, encouraged and supported the development of the region's free zone programs and overall economic development, given the importance of trade and investment in the region. Between 1980 and 1992, the U.S. Government provided approximately \$16.8 billion in bilateral foreign assistance to the Caribbean Basin. The majority of this assistance was implemented through USAID's foreign assistance programs aimed at encouraging industrial development, trade, and investment in the recipient countries.

During the 1992 election year, public outrage over the fact that the U.S. Government was encouraging the development of the manufacturing sector in the Caribbean and Central American countries, thus indirectly supporting the loss of jobs in the United States, came to a head with a 60 Minutes edition that aired on September 27, 1992 and exposed USAID as the primary actor in supporting the "exportation of U.S. jobs, using American tax dollars." Prompted by the concern voiced in the 60 Minutes show, that U.S. foreign assistance might be encouraging the movement of jobs from the United States to the Caribbean Basin, Congress passed section 599 of the fiscal year 1993 Foreign Operations Appropriations Act, prohibiting U.S. government agencies from providing (1) financial incentives that induce businesses located in the United States to relocate jobs overseas; (2) assistance to export processing zones abroad; and (3) assistance to activities that contribute to the violation of worker rights.

PD-20 is USAID's policy providing guidance to USAID missions on how to implement the law. The policy determination states that it is necessary to "undertake an in-depth analysis of the factors which would demonstrate that job losses in the United States are unlikely to occur, either as a result of the relocation of U.S. firms to the zone, or as a result of increased competition from foreign firms operating in the zone which could cause U.S. firms to lose business and consequently reduce their operations."

Specifically, PD-20 asks the question:

"Could the project reasonably be foreseen to involve the relocation of any U.S. business that would result in a reduction in the number of employees of the business in the U.S.?"

While this question cannot be answered very easily, PD-20 provides some guidance as to the kinds of factors that should be analyzed in answering this question. These factors include: whether the recipient country or region is geographically attractive to U.S. firms; whether existing infrastructure is adequate to support external investment; whether normal investment patterns reflect activity in the country by U.S. firms; and whether the types of firms targeted under the project are likely candidates for relocation. The following discussion reviews the attributes of the WBG industrial estate program in light of this question and the factors listed above.

**Geographic Attractiveness
to U.S. Investors**

The West Bank and Gaza is clearly not geographically attractive to U.S. investors. In response to introduction of Section 599 in the 1993 Appropriations Act and to congressional requests to further look into the issue of U.S. tax dollars being used to encourage relocation of U.S. jobs, the General Accounting Office (GAO) conducted an investigation into the matter. In this review of U.S. support for Caribbean Basin assembly industries, the GAO found that one of the primary reasons for U.S. assembly operations to move to an offshore location is access to cheap labor in close proximity to the United States. This conclusion is based on discussions with and site visits to 53 U.S. assembly operators in Honduras, El Salvador, the Dominican Republic, and Costa Rica.¹

The West Bank and Gaza is not readily accessible from the United States, being that it is over 5,000 nautical miles between the ports of Baltimore in the U.S. and Ashdod or Haifa in Israel. The region's remote location is exacerbated by the lack of frequent sea transportation links to the United States, as well as the transit time of 25 to 40 days (depending on the routes and transit ports) required for shipping a container by boat from Israel to the U.S. This factor alone, would preclude most investment from U.S. labor-intensive firms. Increasing competitive pressures and "just-in-time" production and delivery schedules further reduce the attractiveness of the West Bank and Gaza to the U.S. investor in the light manufacturing sector looking for alternative investment locations to produce for the U.S. market.

Moreover, the language barrier is a further deterrent for U.S. investors. While some of the Spanish speaking countries in the Caribbean Basin have done extremely well in attracting U.S. investors, language and proper communication with the work force is always a concern and the Arabic language spoken in the WBG would further complicate the investment process. Given these factors, the West Bank and Gaza is not geographically attractive to U.S. investors in sensitive sectors, such as apparel and shoe manufacturing for instance.

**Review of WBG's
Comparative Advantage**

For low-skill, labor-intensive manufacturing operations, the single most important factor in choosing an offshore manufacturing location is the cost of labor. Other production factors, such as the cost, availability and reliability of basic utilities (water, electricity), and other infrastructure (building cost, transportation), however, are also

Foreign Assistance, U.S. Support for Caribbean Basin Assembly Industries, United States General Accounting Office, Report to Congressional Requesters, December 1993.

important factors in the decision making process during a site location selection process. This section provides a comparative analysis of these factors between the West Bank and Gaza and five countries in the Caribbean/Central American region. For comparative analysis the following countries are used: Costa Rica, Dominican Republic, El Salvador, Honduras, and Jamaica, all of which have successfully attracted U.S. manufacturers in sensitive industries, such as apparel assembly, shoe manufacturing, and low-skill electronics assembly.

Labor

EPZs that have caused a dislocation of U.S. labor have almost always been built on a large supply of cheap labor. Labor costs in such countries targeted by EPZ developers can be as low as \$30 per month, and are usually not much higher than \$120 per month. By contrast, the wage of the least expensive Palestinian laborer is around \$300 per month. As shown in table 3.1 below, the highest manufacturing wage in the successful offshore manufacturing centers in the Caribbean/Central American region is found in Costa Rica, where the hourly wage for a typical assembly operator is \$1.18. Significantly cheaper labor is found in El Salvador and Honduras, where an equivalent worker will earn approximately \$0.60 per hour. In comparison, a Palestinian worker in the West Bank and Gaza Strip will earn approximately \$1.85 for the same work, roughly three times the wage of an operator in El Salvador and Honduras, and still 50 percent more than his or her most expensive counterpart in Costa Rica. See table 3.1 for more detailed information.

Given that salary is the single most important cost factor of a typical apparel manufacturing operation, representing 30 to 50 percent of operating cost, the Palestinian wage rates place the West Bank and Gaza outside the competitive range for U.S. manufacturers looking for alternative offshore locations in the low-skill, labor-intensive industries. There are numerous locations that would be significantly cheaper to choose from, even if all else would be equal.

Transport Infrastructure

One of the West Bank and Gaza's major impediments to foreign investment is its poor infrastructure. During the Israeli occupation there was very little investment in infrastructure in general, and basic industrial support infrastructure in particular. One of the primary reasons for creating the IE program in the WBG is to provide for basic developed industrial land and buildings to accommodate this need. The program will, however, not be able to address the overall poor and inadequate conditions of the road network, and other basic transport infrastructure.

Access to end user markets is the second most important factor in the location decision making process for simple assembly operations. The distance from the WBG to the U.S. market is discussed above; added to this impediment is the cost and time required to ship goods to the U.S. from the WBG. As such, long transit times in shipping connections, costly air freight connections, lack of readily available industrial space, and high cost of other basic utilities are only a few of the most apparent infrastructure constraints. Other than the availability and quality of basic infrastructure is the cost of such services. For instance, shipping a 40 foot container from the West Bank and Gaza to the U.S. costs approximately \$3,350, whereas the same container from the Dominican Republic costs only US\$1,580, or from Costa Rica or El Salvador no more than US\$2,500 – significantly less than from the WBG. (See table 3.1 for further detail.) Transit times from Caribbean ports to the ports of Miami or Baltimore are often no more than a day or two, whereas shipping a container from the ports of Haifa or Ashdod can take anywhere from 25 to 40 days, depending on the routes taken. The cost and time required to ship goods by sea from the WBG is a factor that would weigh heavily against the decision of a U.S. manufacturer to relocate or shift part of its production to the WBG.

The cost of air freight is another factor in selecting a location for simple manufacturing operations. While the majority of finished products in the low-skill, high-labor industries is usually shipped by boat, crucial aspects, such as production inputs, spare parts, new designs, and some high quality, time sensitive fashion goods are increasingly being transported by air. Given this trend, the cost of air freight becomes increasingly important. As shown in Table 3.1 below, the cost of air freight from the WBG to the U.S. is anywhere from two and a half to three times that of an equivalent shipment from the Caribbean/Central American region.

Given the high cost and time factors associated with transporting goods to and from the WBG, it is highly unlikely that a U.S. manufacturer would relocate part or all of its production in the region to manufacture for re-export to the U.S.

Table 3.1: Production Cost Factor Comparison

| Information Category | West Bank & Gaza | Costa Rica | Dominican Republic | El Salvador | Honduras | Jamaica |
|--|------------------|------------|--------------------|-------------|----------|---------|
| Low Skill Manufacturing Wage | \$1.85 | \$1.18 | \$0.82 | \$0.60 | \$0.64 | \$0.83 |
| Ocean Freight Rate US\$/40 ft. container to Miami) | \$3,350 | \$2,415 | \$1,580 | \$2,770 | \$1,965 | \$2,830 |
| Air Freight rate (US\$/lb. to Miami) | \$1.90 | \$0.84 | \$0.61 | \$0.71 | \$0.60 | \$0.46 |
| Electricity Rate (US\$/kwh) | \$0.09 | \$0.06 | \$0.16 | \$0.07 | \$0.09 | \$0.12 |
| Water Rate (US\$/cu.m.) | \$1.00 | \$0.74 | \$0.25 | \$0.37 | n/a | n/a |
| SFB Construction Cost (US\$/sq.ft.) | \$32.50 | \$17.00 | \$23.00 | \$15.30 | \$14.00 | \$20.00 |

Source: Data collected by The Services Group during various field assignments.

Utilities

Electricity. Most electricity in the Occupied Territories (OT) is supplied in bulk from the Israel Electric Corporation (IEC) and sold by local distributors since the Civil Administration and IEC closely control planning, construction and operation of the OT power system. Although most households in the WBG have access to electricity, except for some villages, the quality and quantity of electricity is below what one would expect for an economy of similar per capita income. The inadequacies of electricity supply in the WBG reflect the inadequate investment at all levels of the supply system, from the bulk supply points at IEC substations to the distribution lines feeding the final consumer. Given this poor state of the electric supply in the West Bank and Gaza, power black-outs and brown-outs are frequent and a deterrent to industrial investment.

Electricity rates, while on the higher end of the spectrum are within the competitive range amongst other offshore manufacturing locations. The rate for industrial power during peak hours is approximately \$0.09 per kwh in the WBG, compared with \$0.06, \$0.07, and \$0.09, in Costa Rica, El Salvador, and Honduras respectively.

Water. Almost all people in the urban areas and about 70 percent of the rural population have access to piped drinking water in the WBG; however, the quality of service is far from satisfactory. In the West Bank most municipalities face a shortage of drinking water. Losses in the distribution system are extremely high and most water supply networks are in urgent need of rehabilitation. As is the case with the electricity system, water system extensions have generally been built in a haphazard manner. Wells, the main source of water, need rehabilitation; and many supply mains and distribution lines have to be replaced to reduce leakages and assure adequate water service levels. Needless to say that large amounts of money have to be invested to bring the water supply system up to international standards.

The cost of water in the WBG is high at \$1.00 per cubic meter, as opposed to a range of US\$0.25 to a high of US\$0.75 in the Caribbean Basin. While cost and quality of water supply is not a major factor in the decision making process for a site selection, it is just an indication of the overall poor state of the infrastructure in the West Bank and Gaza.

This brief assessment of the state of the infrastructure clearly shows that the basic infrastructure in the WBG is not an advantage that will attract international investors, but rather a deterrent to investment at this time.

*Traditional Investment
and Market Patterns*

Traditionally the U.S. has been a "natural market" for Israel because it has been unable to trade with its contiguous, neighboring Arab countries. Trade relations between the U.S. and Israel has been facilitated by the U.S.-Israeli bilateral free trade agreement (FTA). Previously, Palestinian Arabs now residing in the West Bank and Gaza have traditionally benefitted from the FTA in two ways: (i) through the migration of a large population of laborers to Israel; and, (ii) as indirect exporters through subcontracting agreements between Arab-owned firms in the WBG areas and Israeli firms. These trade patterns developed over the period from 1967 until the commencement of the "Intifada." It is assumed, but has not been empirically verified, that any impact on the U.S. job market, if any, has already taken place during this period.

In contrast to Israel, the natural market for the West Bank and Gaza Strip economy will most likely be in Israel, due to the facility of trade and customs union with that country, and then other Arab countries such as Egypt, Jordan and the Arab Gulf states.

Statistical information on U.S. investment in the West Bank and Gaza are not readily available and a historical trend analysis is difficult to conduct in this case. Field interviews have shown, however, that while there may be interest from U.S. investors in infrastructure development projects, such as telecommunications, the demonstrated investor interest from light manufacturers for re-export to the United States is non-existent. Moreover, as evidenced by recent investment trends in the region, as well as in Africa, in countries that experience similar problems in infrastructure, and shipping cost and time constraints, as well as the findings of a number of recent market studies undertaken for export processing zone and industrial park projects in other countries in the region and in Africa, interest from U.S. investors in these regions in the area of low-skill, labor-intensive manufacturing for re-export to the United States has been very limited. The majority of U.S. investment in the region is in areas where the U.S. firm is either expanding its markets or seeking to explore natural resources, such as agricultural products and mining and oil exploration. These are not the types of activities that cause a loss of jobs in the U.S. but rather add employment opportunities in the U.S. due to administrative, managerial, and technical support needs of the overseas operation.

*Results of Specific
Market Surveys*

No specific market surveys or feasibility studies have yet been carried out for any of the proposed industrial estate sites in the WBG. These types of surveys will only be conducted as all parties proceed with site selection and development of the project.

The World Bank, however, through a team of Palestinian and Israeli researchers, has conducted a preliminary interview survey² of perceptions and motivation of firms in the apparel, food processing and assembly industries. There were 53 completed interviews (17 overseas Palestinian, 20 Israeli and 16 international). The survey results indicate that the highest areas of concern to all investors before they would be interested in such zones are (1) the free movements of goods, (2) services and people, and (3) the adequacy of the legal framework. Most importantly, for the purpose of this analysis, is that the survey revealed that all the interested companies were looking toward the WBG to locate or expand low-skill operations currently being carried out in Israel in the territories to take advantage of the lower wages in the WBG than in Israel, as well as to overcome the shortage of unskilled low-cost workers in Israel. The

See Annex 3 entitled "Investor Research project for Industrial Estates in the West Bank and Gaza" in the World Bank report, "Industrial Estates and Enabling Environment for Private Sector Development for West Bank and Gaza," June 1995.

majority of the potential investors stated that their production would be to supply to the Palestinian, Israeli and Jordanian populations. A small percentage of the production would also be exported to Europe and the United States. These, however, are not activities that would result in the relocation of U.S. jobs overseas.

An extensive market survey undertaken for the private developer group that is sponsoring the development of Israel's first free processing zone has revealed that there is virtually no interest from U.S. investors in the apparel, shoe, or electronics assembly industry to relocate or expand into Israel. While this was primarily due to the high wage costs in Israel, a major factor that also contributed to this fact was the cost and time required to ship goods between the U.S. and Israel. While it is true that Palestinian wages are as much as half those in Israel, they are still relatively high, compared to other offshore manufacturing locations, and one can safely assume that similar responses would be found in a market survey for the IE program in the WBG, especially since the other investment factors are relatively poor as well, as discussed above.

Summary and Conclusion

Given the relatively high costs of manufacturing in the territories, coupled with the generally difficult conditions for business, the WBG is not an attractive investment environment for low-skill, labor-intensive manufacturing for U.S. investors. The purpose of the IE program in the West Bank is not to attract labor-intensive operations from the U.S., but rather to improve the investment climate in the WBG to provide minimum conditions for successful business operations.

Moreover, U.S. investment in the WBG, if any, would involve business expansion, not relocation, and increase the U.S.'s presence in the international arena of global trade and investment. More than likely, any U.S. investment would likely increase employment in the U.S., albeit modestly. This would result from added technical, administrative, and financial backstop responsibilities based in the U.S. As such the conclusion to this analysis is that there is no reasonable likelihood that relocation of a U.S. firm would take place as a result of the planned industrial estate program in the West bank and Gaza.

Possible Strategies for USAID Support of Industrial Estates In the West Bank and Gaza

Overview

Donor involvement in industrial estate projects has covered an array of approaches including, technical assistance, financing, and operational support. USAID has been particularly active in support of industrial estates as appropriate vehicles for developing countries to promote non-traditional exports and attract new foreign and domestic investment in manufacturing and value-added services. The types of assistance can be broadly grouped into program-related, or assistance to a national program of industrial estates and related institutions, and project-related, or support for individual industrial estates. The following represent the main types of donor or external support provided to assist industrial estate programs, generally on a national level.

The purpose of this chapter is to outline the areas where USAID might assist the IE program in the WBG. The various options are not prioritized in this chapter, but rather outlined in general terms. Our recommended strategy for USAID/WBG involvement and support to the program is outlined in Chapter V, Conclusions and Recommendations.

Program Assistance

Enabling Environment

The legal and policy environment which will support industrial estate development is generally a subset of the overall climate for industrial investment. In the case of the Palestinian industrial estate program, a draft regulation has apparently been prepared. This draft regulation was not made available to the team during our mission, but it is critical now to review this legislation and provide assistance to the PA in finalizing the draft document. Developing this legislation typically can benefit from a comparative examination of other countries' laws and regulations, in order to draw upon the general body of experience and adopt the best international practices to the local context. Technical assistance can be valuable in bringing this comparative perspective to bear, as well as, identifying constraints to manufacturing activities locally which can be addressed in the industrial estate legislation.

In the West Bank and Gaza, introduction of a new legal and policy regime was one of the prospective benefits of establishing and industrial estate program. In other countries, industrial estates are

simply physical entities, without any special legal regime for the firms locating there, or for the developers. In some cases, enabling legislation for industrial estates has been drafted, but is seen as primarily a means to define the character of a parastatal industrial estate corporation, rather than establish a separate policy regime. For example in Jordan, the industrial estates act is essentially enabling legislation for the Jordan Industrial Estates Corporation, although a nominal tax rate concession is included as well.

The context for introducing industrial estates in the WBG is a complicated overlay of existing legislation, planned devolution of autonomy for the West Bank, existing policy of the PA in Gaza, and a framework agreement between Israel and the PA specifically for industrial estates. The elements of this framework agreement are particularly critical. To date, the World Bank has provided assistance in defining this framework and a concept paper has been agreed upon between the Israeli Government and the PA. This concept paper will be presented to a donors' conference scheduled for July 10th in Paris. While progress in drafting the concept paper has been rapid, many details have yet to be defined, and additional short-term technical assistance is necessary to support the rapid enactment of competitive legislation.

The establishment of an industrial estate program in WBG poses unique challenges in terms of the security concerns of Israel that will have to be addressed. This issue will form an integral part of the policy work to be undertaken and will become a component of the overall regulatory and legal environment guiding IE development in the territories.

Institutional Development

As noted in Chapter 3, there are plans to establish an organization to administer and regulate the industrial estate program. The character of this institution has yet to be defined, and is under discussion. Tentatively named the Palestinian Industrial Estate Authority, this body would coordinate various elements of the industrial estate program and implement all aspects requiring government involvement. Technical assistance is often required to make these organizations effective, especially in the start-up years. Long-term advisors are often placed in these institutions to jumpstart the operations and management, and help resolve initial problems. Short-term technical assistance may also provide valuable inputs for organizational development and training. Donor support has also gone to financially supporting the start-up (equipment) and operational costs for a limited period (typically 2-3 years). While most IE authorities can be financially self-sustaining once the programs are established, they seldom are at the outset.

A program of technical and operational support for the PIEA is a major area for donor, and specifically USAID, concentration. Such a project could entail placement of technical advisors in the PIEA for 2-3 years to facilitate start-up, equipping the PIEA with computers, vehicles and other equipment, providing short-term TA on specific issues, training for the staff and management, and possibly financial support for operational costs for an initial, time-bound period.

Investment Facilitation

Promotion of investment in the industrial estates, particularly foreign investment, requires a well-designed program. The Palestinian Higher Authority for the Promotion of Investment, created under the 30 April 1995 Investment Act, is charged with the promotion and regulation of investment in the territories and will require technical support in its implementation. Donor support is often critical to successful investment promotion, from technical assistance in strategy and program design, to institutional development, to funding of start-up and operational costs, including direct promotional costs and promotional materials.

USAID support for investment promotion could encompass all the same components as the institutional support for the PIEA, as well as financial support for promotional materials and specific promotional efforts. While the Investment Act establishes a promotional organization on paper, it is not yet operational and would benefit greatly from donor support in getting established, both in terms of operational funds, and technical assistance and training. A full scale promotion program would be premature at this stage, however, USAID may wish to consider a modest promotion program, possibly done in cooperation with an association of estate developers, in the absence of any other organization.

Export Promotion

As with investment promotion, effective export promotion requires a well-designed program and responsive implementing institution. Export or trade promotion need not necessarily be linked to industrial estates. However, a coordinated promotion effort can bolster industrial estate development, particularly in small countries where key industrial market opportunities are export-oriented.

All of these elements constitute the support framework for industrial development in general, and industrial estate development, in particular, in the Palestinian territories. Donor support modes are well established, and USAID can benefit from its institutional knowledge and experience in these areas. Here again, a major export promotion campaign and institutional commitment would be premature. More modest efforts, perhaps in support of the programs

of chambers of commerce and industry, would be appropriate as an adjunct to other industrial estate assistance components.

Project Assistance

Table 3.1 summarizes the key elements of the donor support programs outlined above. Support for individual industrial estate projects can also be critical. This type of support can be grouped into the following areas:

Project Feasibility Analysis

Each IE project requires a feasibility study to assess its viability from an engineering/physical design perspective, a market perspective, and a financial perspective. For private projects, donors often cost-share or otherwise fund these studies, in order to lower the up-front cost for private investors and help resolve complex technical and financial questions which may otherwise constrain investment. Additionally, prior to the definition of specific projects backed by individual development groups, donors may finance pre-feasibility studies, market and competitiveness analyses, or other pre-investment studies to assess the general viability of industrial estate projects as well as attract interest from potential developers.

The World Bank has funded a preliminary market analysis, and has funds allocated within the TATF for industrial estate feasibility studies. USAID may wish to supplement this effort if demand is evidenced that is over and above what the Bank's program encompasses. Doing so involves a number of considerations. For example, private industrial park developers generally will do their own market analysis and promotion programs, and want to keep the resulting information confidential and proprietary. For example, USAID can set up a co-financing facility, that may match developer funds and allow them to conduct their own studies.

Table 4.1 TYPES OF DONOR ASSISTANCE TO INDUSTRIAL PARK DEVELOPMENT

| | | Mode for Donor Support | Current Status in West Bank/Gaza | Examples of Relevant USAID Experience |
|---|--|---|---|--|
| Enabling Environment | | Technical Assistance; Non-Project Conditional Assistance in support of policy reforms | Subject to negotiations with Israel; World Bank providing STTA Additional STTA required | Cameroon, Kenya, El Salvador, Dominican Republic |
| Institutional Development (Administrative Agency) | | Technical Assistance; Funding for capital and recurring costs | Palestine Industrial Estates Authority under discussion; to be defined; draft law under discussion | Cameroon, Kenya, Jordan, Costa Rica |
| Investment Facilitation | | Technical Assistance to promotion agency; Promotion Campaigns Recurring Costs; Promotional Materials; | No promotion programs at this time; Palestinian Higher Authority for the Promotion of Investment created by the 1995 Investment Act. | Dominican Republic, Honduras, Costa Rica, El Salvador, Jamaica |
| Export Promotion | | Technical Assistance to firms (cost sharing); Technical Assistance to promotion agencies; Promotional Materials; Promotion Campaigns | No organized promotion programs or institutions; highly dependent on Israeli firms. | Kenya, Jordan, El Salvador, Zimbabwe, many others |
| Project Feasibility Studies | | Technical assistance to developers; Generic pre-feasibility studies, market analyses, competitiveness assessments | World Bank Technical Assistance Trust Fund to undertake some feasibility studies; Israel to support one project | El Salvador, Dominican Republic, Belize, Jamaica, Cameroon, Togo, Honduras |
| Developer recruitment | | Technical Assistance; Promotion to investors | Possible role identified | Togo, Cameroon, Dominican Republic |
| Project Financing | | Credit for zone developers | Possible need identified | Costa Rica, El Salvador, Eastern Caribbean |
| External Infrastructure | | Credit or Grant to host country | Preliminary World Bank interest | El Salvador |
| Political Risk Insurance Fund | | Contribution to capitalization of Fund | MIGA sponsorship; draft concept paper in circulation. | El Salvador |

Developer Recruitment

Promotion of investment opportunities in the development of industrial estates is generally a minor component of project support, but one in which donor efforts can be important. There is growing interest among development groups in international projects, generally as joint venture partners with national firms. Bilateral aid agencies, in particular, can assist in identifying prospective partners from their countries, and supporting promotional efforts to inform them of the potential projects and otherwise stimulate their interest. The U.S. government has had little involvement in efforts of this type, which has nevertheless proven valuable in other donor programs. More common to other donor countries' efforts than the U.S., this type of support can be valuable in project viability.

USAID may wish to consider a modest effort aimed at U.S. development firms. It is reasonable to expect that major construction firms, international real estate development firms, and other infrastructure developers who have interests in both Israel and the Arab Middle East would be interested in participating in these projects. The target group of firms likely to be interested is small and readily identifiable. USAID can play a facilitative role in this regard, funding a limited promotion effort that would publicize the project opportunities, and assist development groups with the presentation of their projects to U.S. firms.

Project Financing

Industrial estates require major investments in land, infrastructure and buildings. These require long-term financing, to support project development, at least in most instances. Shortages of long-term finance often result in the development of the sites alone, or on a focus on sale rather than lease of facilities. For the West Bank and Gaza, leased facilities will be important to generating investor interest, in order to reduce their exposure in fixed assets and lower their own capital costs.

In this context, funding of a credit facility, such as a rediscount facility with loans originated by commercial or investment banks, is another important donor function, as with any long term credit. Such support has been typical of many industrial estate programs by both USAID, the World Bank, and other development institutions.

For private industrial estate development, the establishment of a credit facility with the capacity to fund multiple projects will be the most desirable. USAID can draw on its own and other donor experience in developing the parameters for individual loans and the mechanics of collaboration with private financial institutions who would originate the loans. Coverage under the MIGA or some other political risk facility can also be facilitated along with the credit.

These credits can be set up to deal directly with private banks, or via an institution such as the Palestine Monetary Authority.

External Infrastructure

In addition to the costs of developing an industrial park, connections to existing road networks, electricity grids, water supplies, and telecommunications networks can be expensive. In some cases, inclusion of their costs by private developers would make the costs prohibitive, and yet the utilities or public works agencies cannot accommodate the needed investments due to budgetary constraints. Donor funding of these external infrastructure requirements is also a common feature of financial support for industrial estates. With private development of the estates themselves, it is generally set up as a separate credit or funding arrangement directly with the government or responsible agencies.

External infrastructure support will be a natural counterpart to credit for project development. USAID may set up this component either as an adjunct to direct financing or institutional support, or as a stand-alone project. Generally this can be done via the public utilities or other agencies responsible for the infrastructure development. In the case of the territories, this may involve working with as yet to be established Palestinian concerns, rather than with existing Israeli providers.

MIGA Political Risk Fund

The MIGA political risk fund is still in the conceptual stage. Comprehensive political risk coverage will be key to attracting international investment, including foreign joint venture partners for industrial estate developers. The major role for USAID in this case will simply be to contribute to the capitalization of the Fund. Additionally, the U.S. may wish to ensure OPIC coverage for U.S. investments is extended, although this may not be as comprehensive as the MIGA program unless additional features are incorporated into standard OPIC terms.

Conclusions

The purpose of this analysis was not to conduct a full review of the industrial estates program proposed for the West Bank and Gaza, nor to assess the economic viability of such a program, based on cost figures or other competitiveness factors, but rather to review the program as it stands now and to attain a better understanding of the primary issues at hand, especially as they relate to possible future assistance provided to the program by the U.S. Government. As such, the following discussion focuses on issues relevant to making a decision about future involvement in the program by the USAID/WBG mission.

As with all aspects of the peace process, the industrial estate program faces difficulties due to the sensitivities at hand and the security concerns of the Israelis. In the long run, however, implementation of the program should contribute to the overall process of bringing peace to the region and strengthen the foundation of peace in the territories.

The principal conclusions of the study can be summarized as follows:

- **There is strong interest in the IE program for the WBG.** Interviews with representatives from the FA, the GOI, the Israeli and Palestinian private sectors, as well as the international donor community have confirmed that there is good will, strong interest, and support for the rapid development of the proposed industrial estate program in the West Bank and Gaza on all sides. The PA and the GOI have elaborated a joint concept paper that will be presented to the Consultative Group meeting in Paris on July 10, 1995. Assuming a favorable review of the concept paper and a formal request for assistance by the PA, the international donor community is likely to get involved in various aspects of the program.
- **The industrial estate program would address a number of pressing needs and be beneficial to the Palestinian as well as Israeli economies.** Most importantly, the IE program is likely to attract new investment and provide new sources of employment for Palestinian workers. Moreover industrial estates will provide badly needed basic infrastructure for industrial activity, such as access to serviced land with basic infrastructure and buildings. The program will also address

key shortcomings of the legal, regulatory, and institutional environment, which currently hinder investment in the territories. Lastly, the program will address some of Israel's concerns regarding security, by bringing jobs to the workers, rather than bringing the workers to the jobs. As such the program will reduce the need for Israel to import workers, as well as, further reduce the flow of Palestinian workers across the border.

- **Limited studies have been carried out to prove the full economic viability of an IE program in WBG.** A full feasibility study for the program has yet to be carried out to assess its potential economic viability and provide input into the final program configuration. Nevertheless development of serviced industrial land is critical to encouraging investment in the WBG, and moreover, there is a pressing need for a consolidated legal and regulatory framework to support industrial development in the territories. Both of these needs can be met through the development of an industrial estate program within a fairly short time frame.
- **There is strong support from the international donor community to assist the IE program in the West Bank and Gaza.** The interest and commitment of the World Bank in the program is demonstrated by the initial studies conducted by the organization, as well as, the deliberations currently underway in Washington to determine the nature of its future involvement. Bilateral donors, such as the Germans have made preliminary commitments to support the program.
- **Further technical studies are required prior to undertaking physical development of any of the proposed sites.** While the joint concept paper suggests that the PA will seek donor commitments to assist in the development of the nine industrial estates currently proposed, the economic viability and justification for this level of IE development in the WBG has not yet been proven. The market study carried out under the auspices of the World Bank was limited in scope and does not support the creation of over 1.5 million sq.m. of under-roof industrial space as suggested by the concept paper. Even the first phase development suggested by the Bank would yield construction of 350,000 sq.m. of under-roof space, enough for 175 new factories of 2,000 sq.m. each, which would be very ambitious.

- **USAID has experience in supporting similar projects throughout the World. As shown in Table 4.1, USAID has extensive relevant experience in providing technical assistance and support to similar programs throughout the World. This is especially true if USAID is to focus on policy dialogue and support in the area of institution building to support the newly created agencies charged with investment approvals and regulation in the territories.**

ANNEX A

List of Interviewees

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|----------------------|--|
| Abington, Edward G. | Consul General, U.S. Consul General Office, Jerusalem |
| Abou, Hamid | Businessman, Hamid Abou Nil Textile Co., Erez, Gaza |
| Assaf, Nafith | Businessman, Aber El Shamal CO. for Trade and Industry, Jenin, West Bank, |
| Baskin, Gershon | International Director, Israel/Palestine Center for Research and Information, Jerusalem |
| Benvenisti, Refael | Sr. Advisor to Minister of Finance, GOI Ministry of Finance, Jerusalem |
| Bargeron, John | DPO, U.S. Consul General Office, Jerusalem |
| Birnholz, Harry F. | Deputy Director, USAID/WBG, Tel Aviv |
| Blazberg, Noam | Officer, GOI Ministry of Defense, Tel Aviv |
| Brizzard, Jean | Project Manager, PECTAR-Bectel Civil Company, Jerusalem |
| Chamdy, Zion | Economic Branch, Israeli Civil Authority (MATAK) |
| Chokron, Lydia | Deputy Legal Adviser, GOI Ministry of Foreign Affairs, Jerusalem |
| Crowley, Christopher | Director, USAID/WBG, Tel Aviv |
| Efrangi, Abdul Samia | Businessman, Trust Insurance Co., Gaza City |
| Feiler, Gil | Businessman, Info-Prod-Research (Middle East) Ltd., Jerusalem |
| Friedman, Barry I. | Commercial Counselor, U.S. Embassy, Tel Aviv |
| Garber, Judith G. | First Secretary, Economic Affairs, U.S. Embassy, Jerusalem |
| Haddad, Ibrihim | Businessman, Haddad Industries, Jenin, West Bank |
| Hadda, Amin | Operations & Projects, Palestine Development & Investment Ltd. (PADICO), Nablus, West Bank |
| Hajay, Lidenant Col. | Head of Economic Branch, Israeli Civil Authority (MATAK), Erez Zone, Gaza |
| Hanna, Nagy | World Bank Resident Representative Office, Jerusalem |
| Hasboun, Samir | Executive Director, DATA Research & Consulting, Bethlehem |
| Huleileh, Samir | Director, Coordination for NCO's & UN Agencies, Palestine |
| | Economic Council for Development and Reconstruction (PECDAR) |
| Indyk, Martin | U.S. Ambassador to Israel, U.S. Embassy, Tel Aviv |
| Larocco, James | Deputy Chief of Mission, U.S. Embassy, Tel Aviv |
| Mazen, Jerbari | Businessman, Aber El Shamal CO. for Trade & Industry, Jenin, West Bank |
| Mourtaga, Mustafa | Businessman, Mourtaga Trading Co., Gaza City |
| Mullanex, David | Science & Technology Officer, U.S. Embassy, Tel Aviv |
| Odeh, Wajdi T. | Commercial Assistant, U.S. Embassy, Tel Aviv |
| Olsen, Norman | Economist Officer, U.S. Embassy, Tel Aviv |
| Reziq, Nafiz | Businessman, Plastoline Co. Ltd., Erez Zone, Gaza |
| Rothschild, Dani | President, DanRoth, Ltd., Tel Aviv |
| Smith, Timothy | Project Director, D.A.I. Small Business Support Project, Jerusalem |
| Spiegel, Baruch | General Deputy Coordinator, Israeli Activities in the Territories, Tel Aviv |
| Sutphin, Paul | Consul, U.S. Consul General Office, Jerusalem |
| Toren, Bene | Economic Consultant, The Jerusalem Institute for Israel Studies, Jerusalem |
| Yazegi, Mohamed | Vice Chairman, 7-Up Bottling, Gaza City |
| Yazegi, Nasser | Plant Manager, 7-Up Bottling, Gaza City |
| Yerushalmi, David | Chairman and CEO, Israeli Export Development Co., Ltd. (IEDC), Tel Aviv |
| Yose, Foldinger | Businessman, Medical Supply Co., Erez Zone, Gaza |